



THE EUREKAHEDGE REPORT
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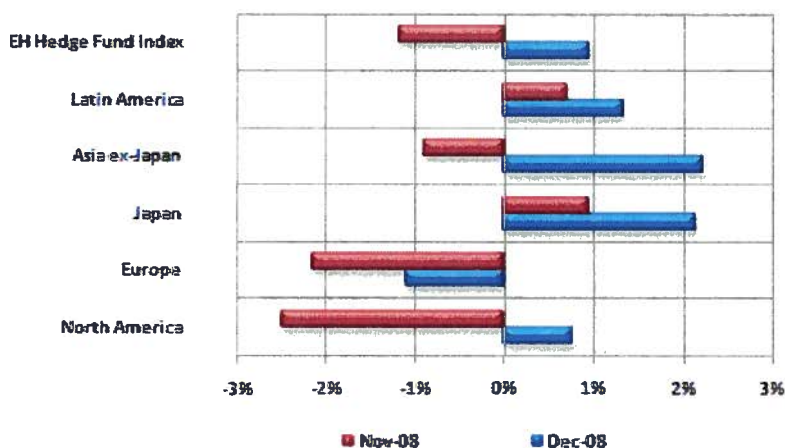
HEDGE FUND PERFORMANCE COMMENTARY – 2008 IN REVIEW

December 2008 Performance

December has traditionally been a positive month for hedge funds, and 2008 was no different; the Eurekahedge Hedge Fund Index returned a healthy 1%¹, positive for the first time since May 2008. The month's gains came despite a continued decline in the global economic outlook in December and negative repercussions from the Madoff scandal. The latter meant that redemption pressures continued to be an issue despite improved performance and the fact that more funds are locking-in their investors during the month; estimated net outflows for December amounted to US\$66.6 billion versus US\$59.3 billion during the previous month. This was offset by an increase in assets to the tune of US\$12.8 billion from gains during the month (in contrast to November 2008 when losses drove total assets down by US\$5.4 billion).

In terms of regional allocations, Asian managers benefited the most from net long exposure in anticipation of a year-end bear market rally, gaining 2.4% as equity indices in Japan, Hong Kong and Korea all rose by 4%. European allocations, on the other hand, were the main detractors from performance during the month, hurt by aggressive rate-cutting by major central banks globally and the resulting spike in volatility. Dwindling liquidity in the equity and credit markets also added to the downward pressure. A comparison of region-wise returns for November and December 2008 are depicted in the chart below.

Eurekahedge Performance Indices - Dec-2008 (Regions)



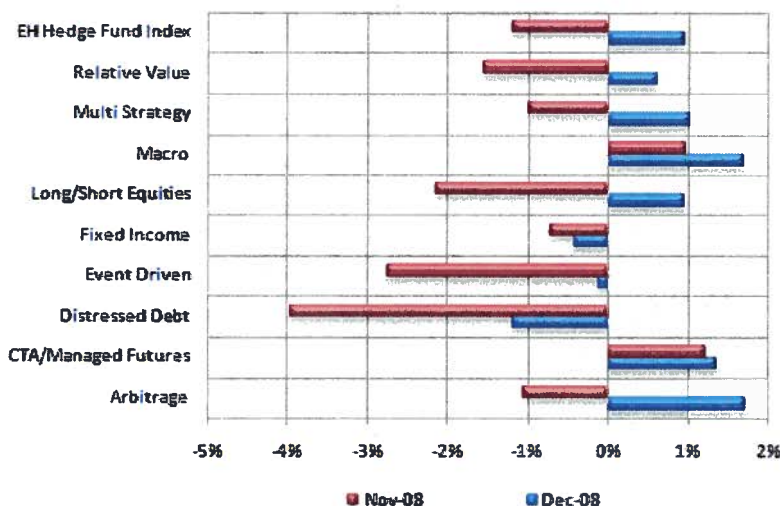
Source: Eurekahedge

Strategy performance in December was dominated by: (a) aggressive interest rate cuts globally by major central banks (the Federal Reserve cut its rate to between 0 and 0.25%, the ECB to 2.5% and the Bank of England to 2%) in a bid to offset weak economic data; (b) ensuing volatility and subsequent rise in equity prices (the MSCI World Index finished the month up 3.1%, the S&P500 rose 0.8%, the FTSE rose 3.4% and the Nikkei 225 returned 4.1%); (c) weakness in the US dollar and the British pound as a result of the steep cuts in Fed and BoE target rates; (d) rising bond prices, as investors reallocated to sovereign debt and yields fell to record lows; and (e) record production cuts by OPEC in a bid to quell the downward trend in energy prices, which was not entirely effective as global demand continued to shrink.

Directional macro (1.7%) and CTA/managed futures (1.4%), and to a lesser extent, equity long/short and multi-strategy (up 1% each) funds finished the month strongly higher, with trend-following proving to be the main driver of the month's gains. Returns from directional equity plays (1.1%) were reflective of underlying equity prices, which remained volatile but ended the month in positive territory. The chart below shows November and December's performance across strategies.

¹ Based on 73.4% of the funds reporting December 2008 returns as at 21 January 2009.

Eurekahedge Performance Indices - Dec-2008 (Strategies)



Source: Eurekahedge

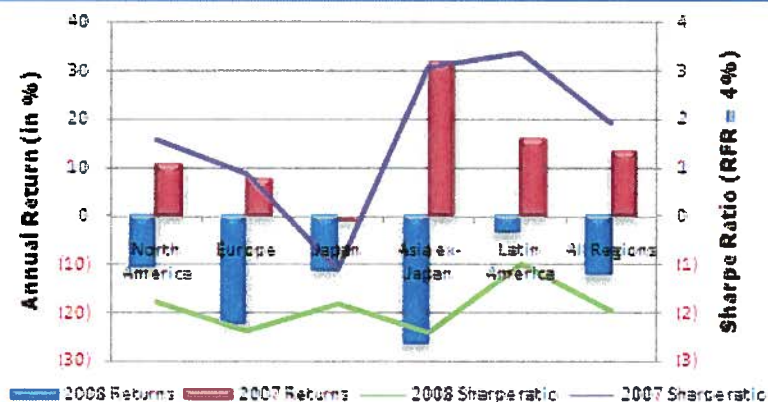
2008 Performance Review

2008 was a particularly rough year for most hedge funds, and stands out as the only negative year in the last nine (as measured by the Eurekahedge Hedge Fund Index). In many respects, the historic and unprecedented market events that transpired between the months of September and November 2008 – the bankruptcy, taking over or bailing out of major, centuries-old institutions in the US and Europe, many of which were service providers to the hedge fund industry, and the attendant pressure to liquidate positions to meet margin and redemption calls in a market already ravaged by subprime and liquidity crises – were quite beyond the control of most fund managers. It is telling that the bulk of the year's hedge fund losses (-12.3%) came about in those three crucial months (-10.7%).

Regional Hedge Fund Allocations

On the year, regional performance has been negative across the board, in stark contrast to 2007. Effectively, funds shed most of, and in some cases more than, the gains made in the previous year. The chart below compares absolute and risk-adjusted returns in 2007 and 2008 across regional hedge fund allocations.

Absolute and Risk-adjusted Returns – 2007 vs 2008 (Regions)



Source: Eurekahedge

The global financial markets were hit by a series of negative economic and corporate data, officially falling into recession in late 2008; the US housing market meltdown precipitated problems in major financial institutions in the region which, over the course of the year, were forced into bankruptcy (most notably, Lehman); had to be bailed out (Bear Stearns, AIG, Freddie Mac and Fannie Mae, among others); or restructured (Goldman Sachs and Morgan Stanley now operate as commercial banks). This was also attended by unprecedented levels of volatility and a crisis of confidence among investors and market makers, leading to a liquidity and credit crunch. The crisis slowly spilled over into other regions, asset classes and institutions across the globe, leading up to a contraction in global demand, and by extension, in commodity prices (most notably crude oil, which saw a precipitous fall in prices from a high of well-near US\$150/barrel to about US\$40/barrel at 2008 year-end).

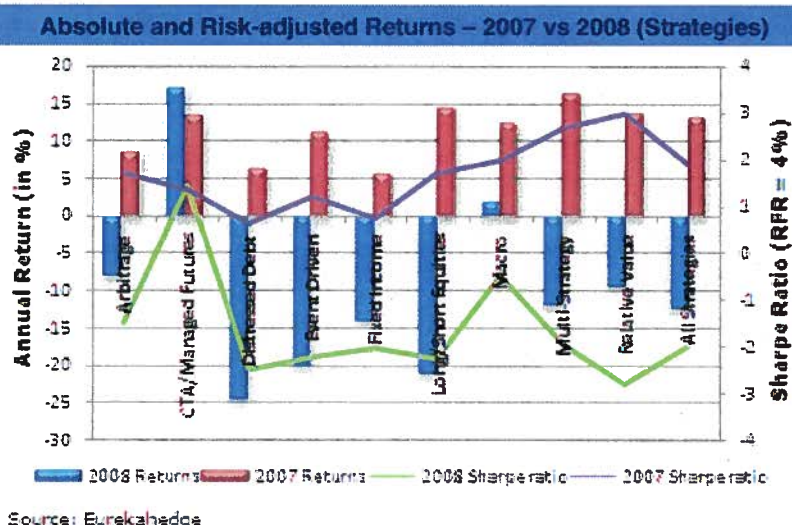
North American funds, which make up slightly under 20% of all funds tracked, were understandably closest to the global average, and witnessed a severe hit to the quality of returns. Risk-adjusted returns (as measured by the Sharpe ratio) fell from a healthy 1.61 for 2007 to a negative 1.77 for 2008, amid wildly fluctuating monthly returns. European managers were similarly riddled by recessionary markets (Germany, Europe's biggest economy, was among the first to declare a recession in November 2008), and lost upwards of 20% on average on the year.

Japan allocations, although not immune to the global downturn, saw the least decline in the quality of returns among all regions. Year-on-year Sharpe ratio fell from -1.08 in 2007 to -1.82 in 2008. Funds in the region benefited from the strengthening of the yen, as yen-funded carry trade positions were unwound globally.

Among emerging markets, Asia ex-Japan managers endured the biggest losses as most economies in the region suffered from institutional outflows and the rush for safe-haven assets. It is promising for investors into hedge funds in the region, however, that funds in the region have not yet fully shed the gains made in 2007. In Latin America, the main decline is in offshore allocations, which are down from US\$43.8 billion in 2007 to US\$30.6 billion in 2008. Onshore allocations remained more or less flat, decreasing from US\$15.4 billion to US\$11.8 billion year-on-year.

Hedge Fund Strategies

In terms of strategies, as has been alluded to in our asset flow review, the star performers were CTA/managed futures and, to a lesser extent, directional macro. This is evident from the comparison of absolute and risk-adjusted returns across strategies in the chart below.



In fact, CTA was the only strategy that saw an improvement in the quality of returns over the previous year in 2008. Funds returned upwards of 17% for 2008, with returns not deviating much from their 2007 levels on a monthly basis. Year-on-year, the Sharpe ratio for CTA funds went up from 1.38 to 1.45. Directional plays were largely profitable on the year, with clear trends in commodity (rising till mid-July, falling since) and currency prices (strengthening US dollar and yen; weakening euro), while heightened market volatility supported the long volatility bias in funds' options portfolios. Macro

strategies were less successful, but still positive on the year (1.8%), and were also the least negative on a risk-adjusted basis (Sharpe ratio of -0.47 for 2008).

Returns across the remaining strategies were more or less uniformly negative with similar risk profiles, as most asset classes could not escape the downturn in the global economy. This was especially true of distressed debt, event-driven and equity long/short funds, as volumes and liquidity dried up in the equity, credit and high-yield markets.

Outlook for 2009

As pointed out in earlier updates, the frequency and magnitude of several government bailout/economic stimulus packages, suggests a more significant role for the government in the functioning of the markets in the months ahead. Furthermore, recently unearthed frauds (such as the Bernard Madoff case) will lend further support to the calls for greater regulation.

Consequently, our outlook for hedge fund performance in 2009 remains cautiously optimistic, as attractive valuations in the equity and credit markets are countered by negative economic data all round and an uncertain investment climate. On the upside, most managers are positioned for an environment of heightened risk aversion and volatility; leverage levels are down and cash levels are up across the board, while an increasing number of funds have restricted or locked down on redemptions, created sidepockets etc in an effort to avoid liquidity constraints and closing positions at a loss.

We expect trend-following and arbitrage strategies in the commodity and currency markets to be profitable in the near term, while opportunistic or value bets in the credit markets (and to a lesser extent, equities) promise longer term gains. The improvement in credit conditions in December 2008 is promising (the 3-month TED spread, the difference between bank and US Treasury borrowing rates, narrowed to its lowest since the Lehman debacle in September).

Furthermore, as indicated in our asset flow review, event-driven and multi-strategy allocations were the only ones that saw positive asset flows in 2008 (US\$8.4 billion and US\$11.8 billion respectively). This is indicative of performance expectations in the year ahead, with allocators betting on diversified and opportunistic plays to generate alpha. In fact, during the course of 2008, hedge fund investors have steadily re-allocated to broader regional and multi-strategy mandates.

Lastly, with fund closures on the rise (upwards of 500 funds liquidated in each of the last three years), new launches on the decline (start-up numbers have been halved the previous years' numbers in 2007 and 2008) industry size back at end-2006 levels (an estimated 8,400 funds managing US\$1.5 trillion), and due diligence more important than ever, consolidation is certainly under way within the industry. But we believe the worst is over in terms of investor redemptions and fund liquidations, given the unlikelihood of the watershed events of 2008 repeating themselves.

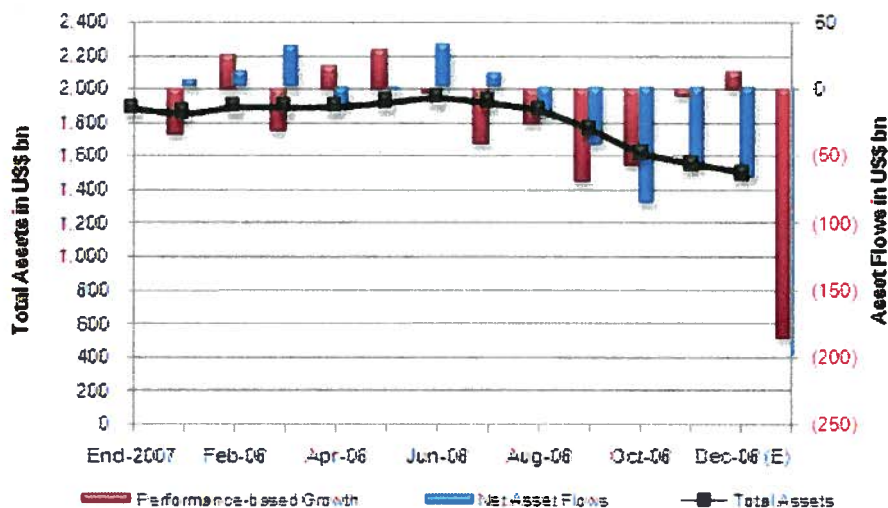
HEDGE FUND ASSET FLOWS – 2008 IN REVIEW

Executive Summary

2008 has been an arguably rough year for hedge funds. Over 20%, or US\$384 billion, has been shaved off the total value of hedge fund allocations globally, and industry assets have dipped below their December 2006 levels (US\$1.54 trillion) for the first time in December 2008 (to US\$1.5 trillion). Investment losses accounted for US\$185 billion of the decline, while net asset outflows from fund liquidations and investor redemptions made up for the balance of US\$198 billion. This is in stark contrast to 2007, when industry assets grew by US\$168 billion on account of performance, and another US\$175 billion from net inflows.

In all, the industry saw positive asset growth from performance in only four of the last 12 months, and net asset inflows in five. Figure 1 below gives a monthly breakdown of industry flows and total assets.

Figure 1: Monthly Changes in Global Hedge Fund AuM in 2008



Source: Eurekahedge

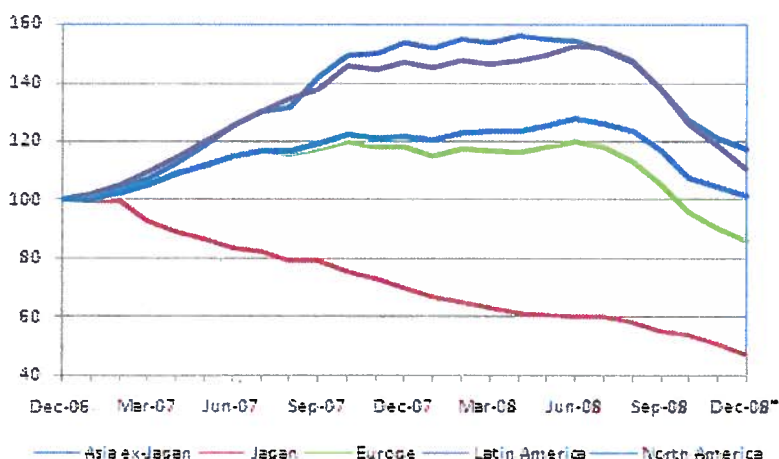
It is generally agreed that hedge funds are expected to preserve capital and/or deliver absolute returns, irrespective of market direction. In this regard, it is crucial to point out that the historic and unprecedented market events that transpired between the months of September and November 2008 – the bankruptcy, taking over or bailing out of major, centuries-old institutions in the US and Europe, many of which were service providers to the hedge fund industry, and the attendant pressure to liquidate positions to meet margin and redemption calls in a climate of declining prices – were quite beyond the control of most fund managers. To corroborate, the composite Eurekahedge Hedge Fund Index was down 12.3% for the year 2008, the bulk of which (-10.7%) could be attributed to those eventful three months.

Regional Allocations

Asset growth among regional hedge fund allocations was largely positive in 2007 and the first half of 2008, but sharply declined in the latter half of 2008, ending the year at or close to pre-2007 levels.

Developed market allocations witnessed the bulk of the decline in absolute terms, while emerging market allocations lost the most in relative terms; North American assets were down 17% on average, while Asia ex-Japan and Latin American assets decline by about 24% each. Japan-focused funds were the exception to this trend and have seen a continued decline in assets over the past two years, with the rate of decline slowing down in 2008.

Figure 2: Regional Asset Growth Index



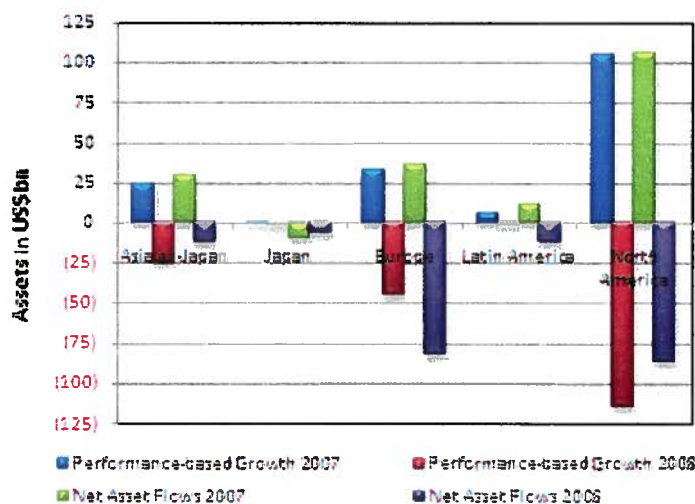
Source: Eurekahedge

The decline in assets was more or less uniformly split between negative performance and outflows, with 2007 and 2008 being near mirror images in either case (refer to Figure 3). But it is interesting to note that among emerging markets in 2008, negative performance was a bigger factor in total asset declines in Asia ex-Japan (US\$24 billion in losses; US\$12 billion in outflows), while it was the opposite case in Latin America (US\$2 billion in losses; US\$12 billion in outflows). This is reflective of much bigger losses in underlying Asian markets, but also of redemption pressures across riskier emerging market allocations in response to the global economic slowdown.

Similarly, redemptions were more responsible for negative asset growth in Europe (US\$44 billion in losses; US\$82 billion in outflows) than in North America (US\$114 billion in losses; US\$87 billion in outflows), corresponding with the nature and volume of negative economic data concerning Europe in recent months.

Japan allocations, on the other hand, lost more from negative performance (US\$0.9 billion in 2007 vs US\$1.6 billion in 2008) and less from redemptions (US\$9.3 billion in 2007 vs US\$6.1 billion in 2008) in 2008.

Figure 3: Year-on-Year Breakdown of Regional Asset Flows



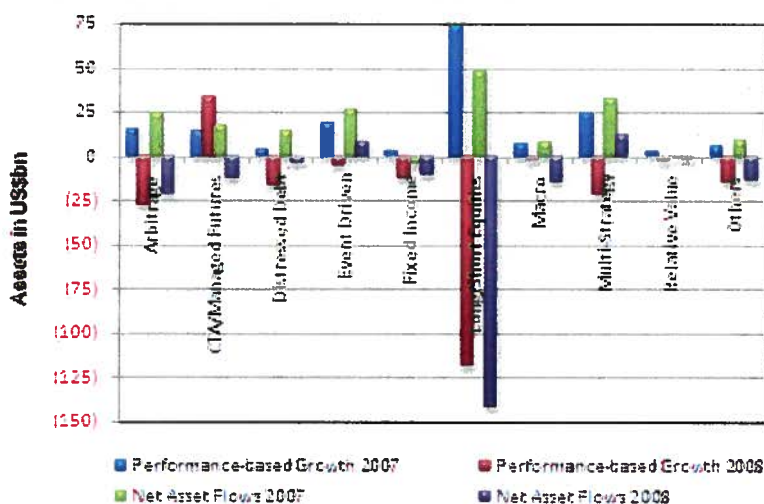
Source: Eurekahedge

Strategy Allocations

Asset growth across investment styles in 2008 was more mixed, as is evident from the breakdown in Figure 4. In terms of performance, the star strategies for 2008 were CTA/managed futures, and to a lesser extent, directional macro, which benefited from clear trends in currency and commodity asset classes across the year. Assets in CTA funds actually grew on account of performance in 2008 (by US\$34 billion), while those in macro funds fell by a relatively marginal US\$2.2 billion. Redemption pressures were also less detrimental to these two strategies, with outflows in each accounting for about 6% (or US\$13 billion) of total industry outflows.

The largest declines in assets was understandably among equity long/short funds (-35%), which accounted for 64% of the losses (US\$118 billion) and over 72% of the outflows (US\$142 billion) in 2008. The heightened volatility and unpredictable markets in the second half of 2008 also took their toll on arbitrage managers, whose assets fell by an estimated 28% (US\$28 billion in losses; US\$21 billion in outflows). Distressed debt and fixed income allocations lost about 24% each as liquidity and volumes progressively dried up in the credit and high yield markets in 2008.

Figure 4: Year-on-Year Breakdown of Asset Flows across Hedge Fund Strategies



Source: Eurekahedge

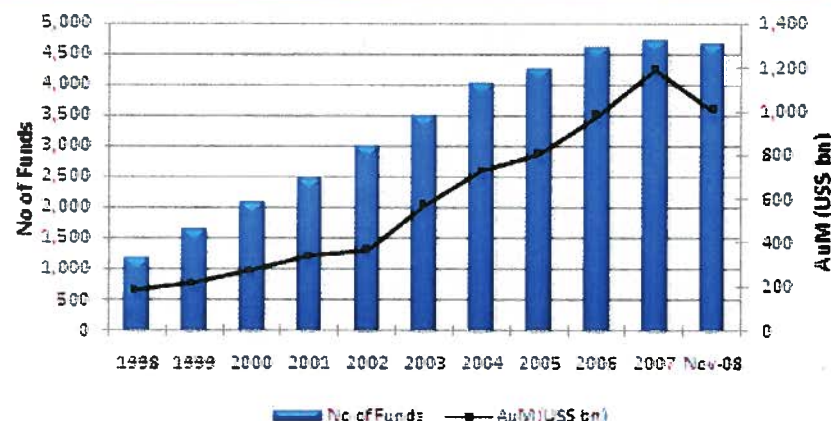
On the flip side, event-driven and multi-strategy allocations were the only ones that saw positive asset flows in 2008 (US\$8.4 billion and US\$11.8 billion respectively). This is indicative of performance expectations in the year ahead, with allocators betting on diversified and opportunistic plays to generate alpha.

2008 KEY TRENDS IN NORTH AMERICAN HEDGE FUNDS

Introduction

The Eurekahedge North American Hedge Fund Database contains data on 3,850 funds¹, based partly on which, we estimate the current size of the region's hedge fund industry at 4,670 funds, managing about US\$1 trillion in assets. This, despite a decline in both the number of funds and assets through 2008, marks an annualised increase of 6% and 12% in the number of funds and AuM respectively, since end-2003. Figure 1 shows the growth in the region's hedge fund space over the past decade.

Figure 1: Industry Growth over the Years



Source: Eurekahedge

While the above chart reflects the growth seen across the industry over the years, it also clearly points out to a drop in the number of funds, and a sharper one in assets, during the first 11 months of 2008. This can partly be attributed to the harsh movements seen across the underlying markets, with centuries-old financial institutions either collapsing, or being taken over, and as a result bringing about record levels of volatility across asset classes and a spike in investor risk aversion. The adverse impact of such movements on hedge fund returns triggered redemptions from the industry, which accounted for a portion of the decline in assets. This fall is further mirrored in the AuM of the industry, which shrank 15.7% for 2008 YTD, compared to the Eurekahedge North American Hedge Fund Index, which lost just 11.3%.

In this write-up, we review recent trends in the size, structure, growth and performance of North American hedge funds, drawing comparisons where applicable to other absolute return funds. To this end, the review is organised to give an overview of various aspects of the current structure of the industry (distribution of funds across strategies, geographical mandates, manager locations, asset-size ranges, etc, and recent changes therein), as also an evaluation of the performance trends shaping this particular space.

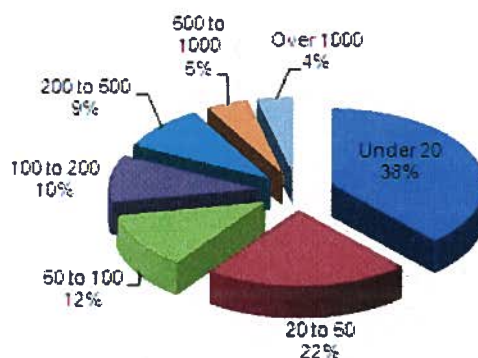
Industry Structure and Trends

Size

The hedge fund universe in North America, if not globally, has been at a 'high-turnover' stage of its industry lifecycle, with many firms entering as well as leaving the market. The rate at which a fund absorbs assets typically depends on the strategy employed, the timing of the investments, as well as a broad 'optimal' size that allows a fund to remain nimble in a dynamic market environment. Taken together, these factors have led to a sustained negative skew in the distribution of funds by size, as is evident from Figure 2 below; nearly three-fifths of the funds surveyed have assets under US\$50 million each, while a mere 4% of the funds manage assets in excess of US\$1 billion.

¹ Including 924 obsolete funds and 76 long-only absolute return funds.

Figure 2: Distribution of Funds by AuM Range (in US\$m)

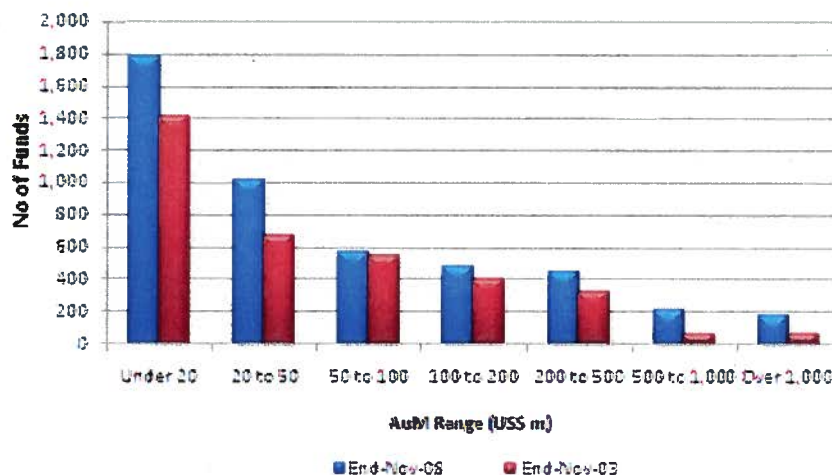


Source: EurekaHedge

While the shares of most of the AuM buckets featured in the above chart continue to remain more or less unchanged from six months ago, the share of funds of under US\$20 million in assets has fallen by 2%, while that of funds with US\$20-50 million in assets has risen by 4%. This suggests that a fairly large number of fund closures seen over the second half of 2008 have been those of small-sized funds (given the difficulty they face in having to meet investor redemptions), while others, which used to fall in the 'Under 20' range, have grown into the US\$20-50 million range, either on account of capital inflows or due to performance-based increases in assets, or both (as seen in CTAs, for instance).

On the other hand, the average fund size has increased over the years, from US\$165 million as at end-2003 to the current US\$215 million (albeit down from US\$252 million as at end-2007), as stable returns during most of the period in question have helped funds progressively outgrow their initial AuM ranges. This transition over the past five years is captured in Figure 3 below. As is evident, medium to large fund sizes (US\$200 million and above) have registered noticeable increases in the number of funds, shoring up fund size averages. To draw a comparison, funds of over US\$200 million currently make up nearly 18% of the region's hedge fund industry, which marks an increase of more than 5% over a 5-year period.

Figure 3: Change in Distribution of Funds by Size in the last Five Years



Source: EurekaHedge

Strategy

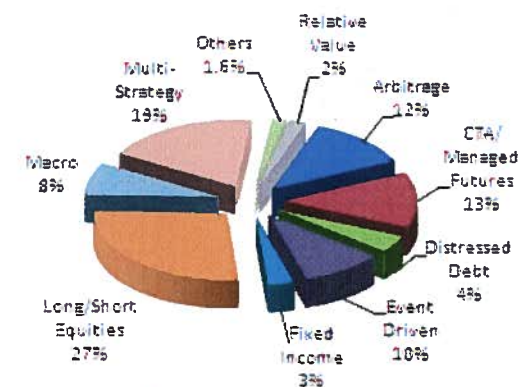
In terms of hedge fund strategies employed, Figures 4 and 5 detail the current breakdown of funds and assets managed. Again, the market shares (both in terms of the number of funds and AuM) of most strategies continue to remain more or less unchanged from six months ago, with CTAs and macro managers being a marked exception.

In terms of assets, the shares of CTAs and macro managers have collectively risen by nearly 8% over the 6-month period, suggesting most of these (which generally tend to go by a 'Global' mandate) to have made good gains from exploiting short-term movements across the currency and commodity markets, thereby attracting fresh capital from investors.

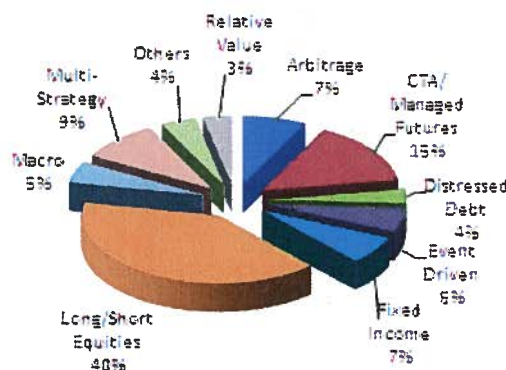
In terms of downward changes, long/short managers have seen their share fall 2%, suggesting assets in the strategy to have shrunk at a higher pace, relative to the industry as a whole.

Figure 4: Distribution of Assets by Strategy Employed

Figure 5: Distribution of Funds by Strategy Employed



Source: EurekaHedge

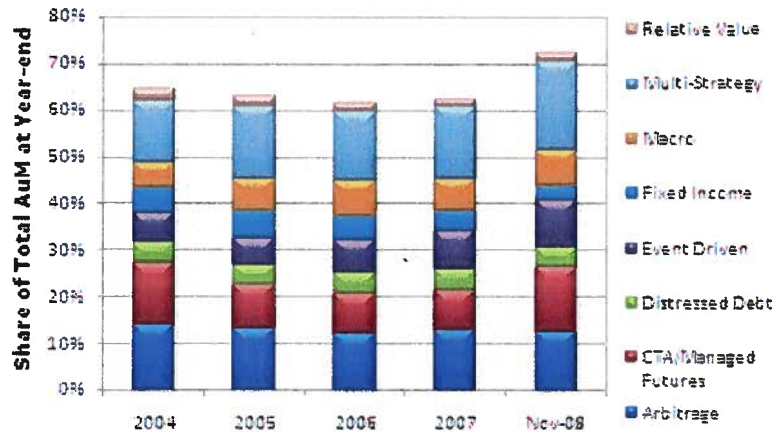


Source: EurekaHedge

Figure 6 shows the year-on-year changes across the market shares of investment strategies from 2004 until November 2008, in terms of AuM managed by North American managers. It must be noted at the outset, that the blank portion in each of the bars (years) represents the market share of long/short equity managers.

Figure 6 shows an interesting relationship between the market share of long/short equity managers and that of CTAs, in the North American hedge fund industry. This, to some extent, suggests that investors churn their capital across the two strategies cyclically, based on how they (and the underlying asset classes) are performing. For instance, when the underlying equity markets rallied until mid-2007, the share of long/short managers grew at a steady pace, while that of CTA/managed futures managers fell; and vice versa, for the 11 months of 2008.

Figure 6: Change in the Strategic-mix of the Industry

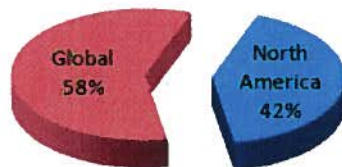


Source: EurekaHedge

Geographic Mandate

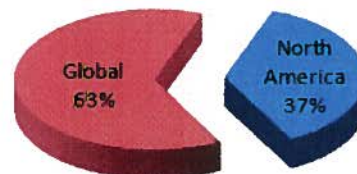
This review looks mainly into funds that allocate to North America, and does not particularly include data on funds that are merely based in the region but invest elsewhere. So, to that end, we have put together two pie charts to compare how the mix between the two geographical mandates that allocate to North America (namely 'Global' and 'North America') has changed over the 11 months of 2008.

Figure 7: Geographical Mix (end-2007)



Source: EurekaHedge

Figure 8: Geographical Mix (Nov-2008)



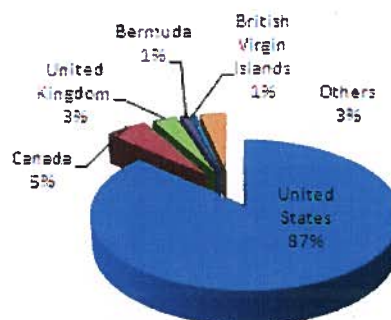
Source: EurekaHedge

With a quick glance, one can infer a distinct (5%) increase in the share of global-mandated funds investing in North America, and an obvious corresponding decrease in the share of funds focusing only on North America. This can be explained by the increased demand for funds with a broader focus, as opposed to single-country/single-region managers, as a measure for investors to reduce risks associated with being over-exposed to a single region during times of economic uncertainty. We will look at how this strategy has worked for investors, in the performance section of this report, by comparing the returns realised by funds employing both the aforementioned geographical mandates.

Manager Location

In terms of manager locations, it is needless to mention that the US is home to a majority of the funds allocating to North America. As Figure 9 illustrates, the US and Canada collectively make up over 90% of the North American fund population, while locations other than the top 5 account for a mere 3% of the funds.

Figure 9: Top 5 Manager Locations (by No of Funds)

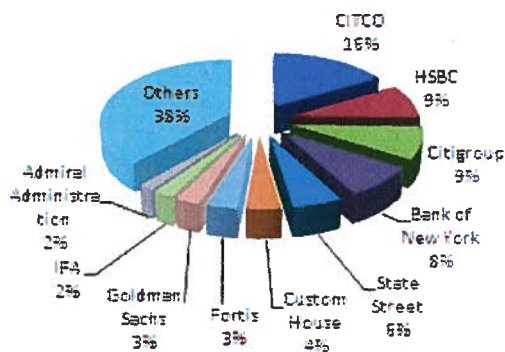


Source: Eurekahedge

Service Providers

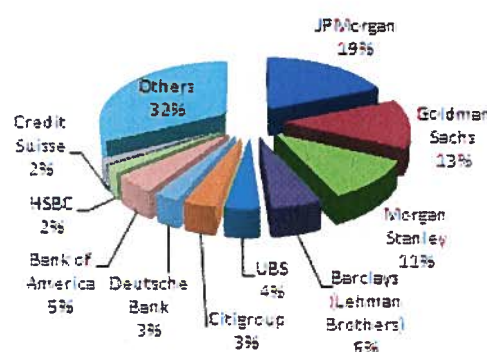
Here, we look at the current market shares of service providers² to North American hedge funds. Figure 10 provides a snapshot of the shares of the top 10 hedge fund administrators (by assets under administration), while Figure 11 shows the same for prime brokers (by their assets under management). Interestingly, both the breakdowns show that the top 10 service providers account for between 60% and 70% of the business in the region.

Figure 10: Top 10 Administrators (by AuM)



Source: Eurekahedge

Figure 11: Top 10 Prime Brokers (by AuM)



Source: Eurekahedge

Performance

North American hedge funds have traditionally offered among the most stable returns (annualised returns of 9.5% with a Sharpe ratio³ of 0.9, since January 2000). But how do these returns compare against those of hedge funds allocating to other regions?

In order to answer this question using a fair comparison, we have worked out the dispersion of the 36-month annualised returns of funds allocating to different regions – Asia, Europe, Latin America and North America – followed by a similar comparison across the different types of investment vehicles that allocate to North America. It must be noted at the outset, that for Latin American hedge funds, we have only considered the returns of offshore managers, since most of their onshore counterparts tend to have their funds denominated in the Brazilian real, of which the marked appreciation

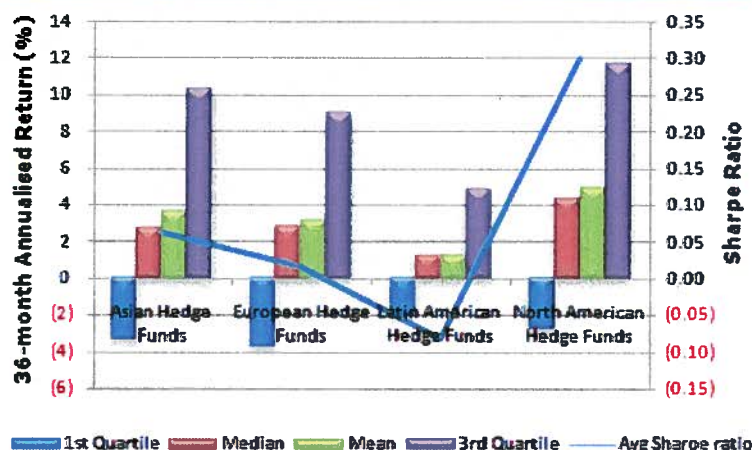
² Based on the funds reporting their data to the Eurekahedge databases.

³ All Sharpe ratio calculations have been calculated using an annualised risk-free rate of 4%.

against the US dollar in recent years, tends to positively skew the average returns for the region.

Figure 11 shows that North American managers have recorded the highest average, median and 3rd quartile returns as well as the highest risk-adjusted returns for the 3-year period ended November 2008. These returns point towards the impressive return-generating potential of North American managers (which, to some extent, is a function of their experience and expertise), especially when one takes into account that North America, and particularly the US, has been among the worst-hit economies in the recent (and ongoing) global economic crisis. No doubt, they also exhibit among the largest inter-quartile ranges, but that can be justified by the sheer population in the North American hedge fund space (which, in terms of the number of funds, makes up over 50% of the global hedge fund industry).

Figure 12: Dispersion of 36-month Annualised Returns (Regions)

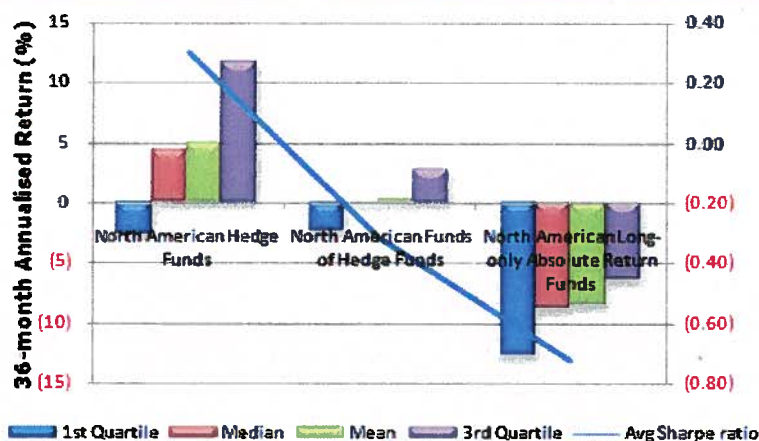


Sources: EurekaHedge

In terms of returns across different fund types allocating to North America, hedge funds have clearly outperformed – both in terms of returns, as well as their Sharpe ratios, with their long-only counterparts having fared the worst, given the poor performance of the region's equity markets, coupled with the relatively higher beta that long-only managers generally provide.

Funds of North American hedge funds have underperformed single managers, owing to factors such as the fee component of the returns they generate (that is, not only do they charge their own performance fees, but they also pay incentive fees to the underlying hedge funds that they invest in, which results in considerably lower net-of-fees returns). Furthermore, with a rather wide dispersion of returns across single-manager funds, particularly in 2008, funds of hedge funds were faced with a challenging task of manager selection; in many cases, gains realised from hedge funds employing trend-following strategies like CTA/managed futures and macro were offset by losses from opportunistic hedge funds employing strategies like long/short equities, among others.

Figure 13: Dispersion of 36-month Annualised Returns (Fund Types)



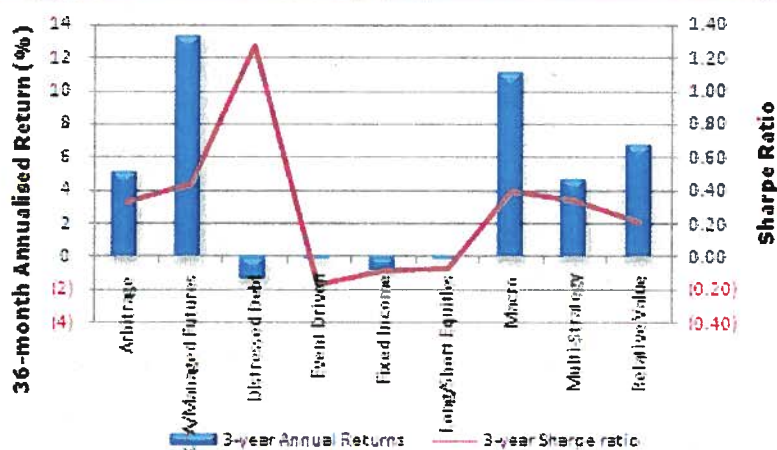
Source: EurekaHedge

Having established that North American hedge funds are among the best performers over the last three years, we will now look into the average 3-year annualised returns across the different geographical and strategic mandates employed by managers investing in the region.

Figure 14 illustrates the 3-year annualised returns and the Sharpe ratios across the different strategies employed by hedge fund managers allocating to North America. In terms of returns, CTA/managed futures and macro managers have recorded double-digit gains, largely owing to an impressive year in 2008, while most other strategies took a considerably hit. Both CTA/managed futures and macro managers made decent gains from short-term currency and commodity trading through most of 2008, thereby adding on to their past-year gains, while other strategies like long/short equities and event driven, among others, were adversely impacted by the record volatility and sharp downturns in equity markets; the S&P 500 was down 34% as at end-November 2008.

As for risk-adjusted returns, those of distressed debt managers have been widely (positively) skewed by the Sharpe ratio of one fund (which returned 28% per unit of risk); excluding the abnormal number of this fund, the average Sharpe ratio for the strategy falls to -0.4. As was the case with returns, CTAs and macro managers also have the highest Sharpe ratios for the 3-year period ended November 2008, while long/short, event-driven and fixed income managers recorded the lowest (again, mainly due to their 2008 losses at -17.8%, -26.2% and -10.8% respectively, up to November 2008).

Figure 14: 36-month Annualised Returns across Strategies



Source: Eurekahedge

When looking at a similar comparison for the two geographical mandates with exposure to North America (namely Global and North America), we see that the 3-year annualised returns of the broader Global managers are more than double those of pure-North American managers, who have a relatively narrower geographical focus. This can be explained by a simple fact – that most CTA and macro managers (the only two strategies to have posted double-digit 3-year annualised returns, as shown in Figure 14) tend to employ a global mandate. Furthermore, the number of pure-North American long/short managers is nearly twice the number of Global long/short managers allocating to North America; and, the losses of long/short managers in 2008 offset a significant portion of their preceding years' gains, which are reflected in their relatively lower 36-month returns.

Likewise, Global managers have also yielded twice the returns per unit of volatility, as compared to their pure-North America-investing counterparts. This goes some way in reiterating the point mentioned in the "Geographical Mandates" section of this review, explaining why the demand for managers with a broader regional focus (and hence, presumably a more geographically diversified portfolio) has increased over recent times, while that of single-country/single-region managers has seen a corresponding decline.

Figure 15: 36-month Annualised Returns across Geographical Mandates



Source: Eurekahedge

In Closing

North American hedge funds, on the whole, have fared notably better than those investing across most other regions in the past year, with the Eurekahedge North American Hedge Fund Index having lost 10.6% through 2008. This compares well with the underlying markets, where the S&P 500 lost 33.5% for the year, crude oil closed the year down 54%, and most major currencies recorded double-digit percentage declines against the US dollar.

On a micro level, however, several funds did take a hit during the year, owing to the turbulent markets, distress across credit markets and investor redemptions. These factors are likely to continue to put pressure on the industry over the months to come. However larger managers have an added advantage of being able to diversify their assets geographically, and maintain a fair portion of their portfolio in cash in order to meet redemptions. Small funds, on the other hand, with their inability to do so, could run the risk of either being unprofitable (in case they hold a large portion of their portfolio in cash) or suffering losses (in case of having to liquidate holdings unexpectedly to raise cash levels). In this light, we believe that the current stress in the industry might, on some level, work as a filtration process and even threaten the survival of some small and inexperienced managers, particularly over the near term. Having said that, we expect to see more hedge fund start-ups over the near future, given the increasing number of people moving out of investment banks (whether voluntarily or otherwise) to venture into the hedge fund space.

In terms of returns, we believe that hedge funds are in a better position to generate superior returns than most other conventional managers and market players, owing to the flexibility that hedge fund managers enjoy, and their ability to identify new trends and investment ideas and act on them promptly. We anticipate trend-following strategies to continue benefiting from market movements across the currency and commodity markets, as they had through most of 2008. We expect the equity markets to remain volatile and range-bound over the next few months, but long/short managers could potentially benefit from pockets of opportunities (even if short-term ones) on both the long and the short side, given the uncertainty around the 4Q08 earnings reports and deeply discounted valuations across most sectors.